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SUBJECT: AZERBAIJAN: AMBASSADOR MANN TALKS ENERGY WITH
PRESIDENT ALIYEV

Classified By: Ambassador Anne E. Derse, (reasons 1.4 b,d)

¶1. (C) SUMMARY: President Aliyev seeks enhanced cooperation with Turkmenistan on offshore energy development, and is willing to be minority partner with the GOTX in developing the Serdar-Kapaz field. Aliyev seeks concrete action from Turkmenistan showing it is interested in such cooperation, and agreed that GOTX approval to be part of a USTDA feasibility study on cross-Caspian gas transit would be such a step. Eurasian Energy Coordinator Mann said President Aliyev and Azerbaijan could provide a good example to Berdimuhamedov of both how to invite foreign energy companies into a productive partnership, and how to conduct balanced relations with Russia, and urged Aliyev to strengthen his relationship with Berdimuhamedov in order to facilitate bilateral cooperation. Mann and Aliyev agreed on the need for BTC expansion to 1.8 million barrels a day and possibly a 'second BTC' to handle increased Kazakh oil volumes. In this regard Mann urged Aliyev to approve intermediate BTC expansion to 1.2 mmbd. Aliyev said GOAJ is concerned about possible GOAJ financial losses and is delaying approving intermediate expansion to 1.2 barrels a day until the ACG Partners "clarify the situation." Aliyev said that currently Azerbaijan has "no gas for Georgia," but that if the ACG Partners were to re-inject less, it could provide Georgia with gas. On gas transit through Turkey, Aliyev repeated that the GOT insistence on its 15 percent netback scheme was preventing timely pursuit of commercial contracts for Azerbaijani gas. END SUMMARY

¶2. (C) On February 25 Ambassador for Eurasian Energy Diplomacy Steve Mann and Ambassador Derse met with President Aliyev to discuss energy issues. Also present were USTDA Regional Director Dan Stein, USTDA Azerbaijan Desk Officer Jamie Merriman, and Embassy Energy Officer.

NEW POSITION

¶3. (C) Ambassador Mann said in his new position as Ambassador for Eurasian Energy Diplomacy he will be coordinating the USG effort on energy, working as part of a team with analysts and policy-makers in Washington and with Ambassadors in the field. Mann noted EUR DAS Bryza's depth of knowledge on energy issues and advised that he would continue to play a special role and continue as the lead on Nabucco and in handling the European gas downstream.

¶4. (C) One specific focus of Mann's would be Turkmenistan, which he thought was "in play." This was a "fascinating time" for Azerbaijani energy development. The first phase was focused on the "Contract of the Century" the second phase would focus on dealing with new volumes, from Shah

Deniz Phase Two, ACG DeepGas, Kashagan and Tengiz, plus (hopefully) Turkmenistan. President Aliyev was happy to hear of Ambassador Mann's new position - "it is good you are back, because we can't do it ourselves." The energy situation was more complex now than at the time of BTC's conception - there were "more players, and it is more difficult to bring these players together."

SOUTHERN CORRIDOR

15. (C) Aliyev said Europe must understand that Azerbaijan can provide "large gas volumes." Not only was there Shah Deniz Phase Two (SD2), but also the Inam field was currently being developed. Azerbaijan's providing energy to Europe will create a "new psychology" in Kazakhstan and Turkmenistan, showing them that sending Caspian energy westwards (vice through Russia) "doesn't depend on them; it'll happen anyway." It was imperative to bring together all elements, to include Central Asia, Turkey and the European Union. Azerbaijan should lead the process ("we must be the coach and the captain"), since it was "in the middle" and both a producer and a transit country. It also had the experience that Europe and Central Asian countries lack, and has all the infrastructure and relating agreements in place. Aliyev cautioned that time was of the essence: "if we lose time, we lose the game." In this regard, solving gas transit through Turkey was crucial, since once that issue was resolved, Azerbaijan could start "serious negotiations" with other countries.

16. (C) Repeating that "we have the gas," Aliyev said Socar has increased its domestic gas production twice. Azerbaijan was currently producing a total of 27 billion cubic meters (bcm/a) annually (Comment: inside and outside the PSAs). BP

would re-inject 11 of those 27 bcm into the ACG field. "BP doesn't want to give us this gas for free," which is why they are re-injecting it. Returning to one of his favorite themes, distrust of BP, Aliyev said that "I don't know BP's agenda..they are active in Russia...there are rumors...I have my suspicions..." Aliyev said that if there were agreements in place, "Nabucco would have gas today." Azerbaijan has "17 to 18 bcm/a available for sales" (Comment: it is unclear where President Aliyev is getting these numbers, unless he assumes that all ACG associated gas is available for sale).

17. (C) As for ACG Deep Gas, Aliyev said "Azerbaijan will do it," i.e. SOCAR, vice BP. This way Azerbaijan will not have to apologize for BP's performance failures, as it did when Shah Deniz Phase One had start-up delays. SOCAR will also start the offshore drilling Umid-Babek field soon - "we can do it easily, and easier for you to work with us since there is no consortium." (Comment: According to BP, SOCAR is technically unable to develop ACG Deep Gas. Additionally, according to the terms of the PSA the ACG Partners, who have the right of first refusal and the right to match any offer on the table to develop ACG Deep Gas, can for all intents and purposes prevent anyone else from developing it until the PSA runs out in 2024. As for SOCAR's developing Umid, BP points out that SOCAR, under tremendous pressure from the President to have a "success," are developing only a small portion of the field, with negligible amounts expected to be extracted).

18. (C) Aliyev said his recent trip to Hungary was good, although he described Hungarian officials as "slow and hesitant." Nabucco was key for Hungary (Comment: this meeting was held the same day as the Russia and Hungary agreed to cooperate on the South Stream Gas Pipeline project). The Bulgarian President would be coming to Azerbaijan in early March as part of a regional trip. Ambassador Mann said that the USG had encouraged Bulgaria not to sign up for South Stream, or to do so only with serious "red lines," but "Bulgaria was weak." Pointing out that the USG "continues to support Nabucco as part of a range of alternatives," Mann urged support and said that GOTX commitments to send new volumes west would be an important

step.

GEORGIAN GAS

¶9. (C) Aliyev said Georgian President Saakashvili has been seeking more additional gas from Azerbaijan, but "we don't have any gas for them." The only Azerbaijani source for additional volumes would have to come from the 11 bcm/a the ACG Partners are currently re-injecting - "if BP were to re-inject 10 instead of 11 bcm/a, Georgia's problem would be solved." BP won't consider this option, since its bottom line is profit, whereas Azerbaijan's bottom line is strategic. Hence, Azerbaijan sold gas to Georgia in the lead-up to the recent Georgian elections, even though doing so cost Azerbaijan USD 25 million dollars. Barring additional associated gas from the ACG field currently being used for reinjection, if Azerbaijan were to sell additional volumes to Georgia without taking any financial losses it would have to charge a price of USD 300 per thousand cubic meters (tcm) to compensate for the cost of burning mazut in place of the lost gas.

TURKISH GAS TRANSIT

¶10. (C) Concerning gas transit through Turkey, Aliyev said Turkey would eventually have to act in accordance with international practice. He criticized Turkey for cutting off gas supplies to Greece, contrasting it with GOAJ behavior - "even though we had the coldest winter in 75 years, we held to all our gas commitments." Turkey's gas cut-off of Greece undermined what Turkey, Georgia and Azerbaijan had achieved together, and had helped Gazprom. Aliyev stressed that, as in the past, Azerbaijan would always live up to its supply commitments.

¶11. (C) Ambassador Mann said that Azerbaijan has proven that it is indeed a reliable supplier. On Turkish transit, Ambassador Mann shared Azerbaijan's "bemusement" at the GOT 15 percent netback scheme, which both consumers and producers were telling him was "not sustainable." Decision-making in the Turkish energy sector was "complicated, but now that Botas had a new management team in place, it was moving ahead on TGI. What was notable was that Turkish gas demand has grown back strongly to the point where it is a consuming,

vice transit, country, Ambassador Mann said perhaps what is needed is a re-affirmed set of commitments from Azerbaijan to Turkey on gas supply (take or pay).

KAZAKHSTAN& BTC

¶12. Ambassador Mann said he recently saw KMG Chairman Uzakbay Karabalin, who pointed out (with regard to Russian subsea objections) that there are already six thousand kilometers of pipe in the Caspian. The Kazakh government has "already solved the Kashagan issue, and the second generation of TCO, which will double its production volume, is almost finished. CPC expansion "is going nowhere," all of which means that cross-Caspian is the preferred route for coming Kazakh oil volumes. As such, Ambassador Mann encouraged strengthened Azerbaijani-Kazakh ties, and urged that the two "not create new bottlenecks" that would hinder the westward flow of Kazakh oil. In Astana, he warned that Kazakhstan should not become "a new Transneft" in its construction of pipelines; he cautioned both Kazakhstan and Azerbaijan to avoid attempts "to monopolize the trans-Caspian fleet" - both sides must cooperate and work it out in order to make the cross-Caspian oil transportation profitable.

¶13. (C) Referring to stories that the GOAJ was seeking to delay expansion of the BTC pipeline from 1 to 1.2 million barrels per day, Ambassador Mann said BTC expansion was imperative. President Aliyev said the GOAJ was ready to work constructively on this issue. The GOAJ agrees to the principle of BTC expansion, but there are concerns and "we

need to find a compromise." Expansion at this time would cause SOCAR to incur financial losses. Azerbaijan was seeking answers from the ACG Partners, and once the situation was clearer, it will be easier for the GOAJ to make a decision.

¶14. (C) President Aliyev reaffirmed his desire that Azerbaijan be a transit country. It is working with the Kazakh government and with private IOCs, to include Chevron, whose board of directors recently traveled to Azerbaijan. Azerbaijan had a number of projects being finalized that would enhance regional cooperation. It was firmly committed to all the agreements of which it was a party, and was now focusing on the related financial issues.

¶15. (C) Ambassador Mann replied that if large monetary amounts were involved, then by all means the GOAJ should engage in "tough discussions," but if the amounts were small he urged the GOAJ to "stay strategic." BTC must eventually expand to 1.8 mmbd, and all concerned must keep an open mind to the possibility of a second BTC in the future. President Aliyev agreed, saying "we are thinking the same way."

TURKMENISTAN

¶16. (C) Ambassador Mann called energy link-ups between Azerbaijan and Turkmenistan "critical." Mann said that during his upcoming visit to Ashgabat, he would be asking President Berdimuhamedov if USTDA could add the topic of westward movement of offshore Turkmen gas to the existing feasibility study that SOCAR was administering covering possible oil and gas pipelines from Kazakhstan to Azerbaijan.

Mann explained that when previously asked this question in mid-2007, the GOTX had demurred, saying that it was waiting for progress on delimitation. However, Ambassador Mann said the thought the situation in GOTX has changed since then. This feasibility study would not be on a "Trans-Caspian pipeline" from Turkmenistan; it would instead focus on a "early gas" approach.

¶17. (C) Aliyev said that if Turkmen President Berdimuhamedov were to agree to have the USTDA study include Turkmenistan it would be an "important step," and a "serious breakthrough." Azerbaijan already had the existing infrastructure, and stood ready to provide maximum assistance to the GOTX. The GOAJ was a good example of the fact that relations with Russia were not impaired by an independent energy policy, and that the GOAJ has cooperative and friendly relations with Russia now.

¶18. (C) Aliyev said that the GOAJ has striven to normalize relations with the GOTX since Berdimuhamedov's ascension, to include high-level bilateral meetings and telephone calls, settling the bilateral debt issue and seeking to re-open the GOTX Embassy in Baku. There have been many positive developments in a short amount of time, but "now was the time

to hear Turkmenistan's plans. "We need more than good intentions;" now Azerbaijan needed to see the GOTX take some steps - "it is a time of clarification." If the GOTX agrees to an interconnector, the two countries need to have a plan. Ambassador Mann said that expansion of the USTDA feasibility study is the concrete issue to test the GOTX's intentions, and that after his coming meeting with Berdimuhamedov he hopes to have a green light.

BERDIMUHAMEDOV

¶19. (C) Mann said he had met with GOTX President Berdimuhamedov six times since the previous March. Berdimuhamedov understands the magnitude of the problems inherited from Turkmenbashi and wants to fix them, but doesn't know how. He seems sincere but doesn't volunteer his opinion, and his demeanor is probably the result of survival skills that served him in good stead during the Niyazov era. As he is unfamiliar with public policy, he chooses to

continue Niyazov's policies until other options become clearer. Mann said he was hopeful that Berdimuhamedov was currently reviewing existing policies with an eye towards reform. Evidence of such intent could be seen in Berdimuhamedov's "radical" decision to unify of the dual exchange rate the previous November.

¶20. (C) Mann has talked with him and with the GOTX Foreign Minister Meredov a lot about delimitation issues, telling the President at one point that "no one else uses their land-based methodology for delimitation." The previous August the Foreign Minister said Turkmenistan "needed to revisit its delimitation policy." However, it is hard for Berdimuhamedov to renounce Niyazov's "far-reaching" delimitation claims with its corresponding abandonment of potentially billions of dollars of revenue

¶21. (C) In response to Mann's question about his impressions of the GOTX President, Aliyev said he found him a "closed, distant man." During biannual CIS meetings, when participants tend to be informal and joke around, he is not part of the group and stays "silent, always silent." Aliyev said he had a good meeting with him in St. Petersburg, and that he seems to want to change Turkmenistan's image and status, integrating it into the regional and international community. Aliyev said Turkmenistan needs an active reform program, but it would be hard to make radical changes - "they have a strange country." He agreed with Mann that Kazakhstan and Azerbaijan could provide attractive examples to Turkmenistan of countries successful implementing "step by step changes." Berdimuhamedov should be told that reforms would not damage his power, but that "when people are dissatisfied, you lose control." Modernization means moving towards Europe and working with institutions such as the EU and the Council of Europe ("although they can be a headache"); the alternative was becoming "more like Pakistan."

¶22. (C) Thanking President Aliyev for these insights, Mann said that he thought that Turkmenistan could be brought into useful negotiations, but that everything they achieve would be based on the personal relationship between the two presidents. The key to improved bilateral relations was the relationship between Aliyev and Berdimuhamedov. President Aliyev and Azerbaijan could provide a good example to Berdimuhamedov of both how to invite foreign companies into a productive partnership, and how to conduct balanced relations with Russia. It would be good for Berdimuhamedov to receive advice from Aliyev vice the USG, since when the USG speaks in this part of the world, many think its motivation springs from "East-West competition." Referring to Berdimuhamedov's invitation to Aliyev to visit Turkmenistan, Mann urged that Aliyev confirm "both dates at once," i.e. his Head of State visit to Turkmenistan, and Berdimuhamedov's Head of State visit to Azerbaijan.

¶23. (C) In this regard, Aliyev agreed that if the two countries unite their efforts, both will become stronger, and said he would work to improve his personal relationship with Berdimuhamedov. However, he pointed out that when Berdimuhamedov became President, he visited all the neighboring countries, except Azerbaijan, and as such from a protocol point of view, as the most junior CIS President, he needed to come here" before Aliyev could visit Ashgabat.

¶24. (C) On delimitation, Aliyev said the GOTX must "be realistic and step back from their unrealistic claims" on the ACG Field - "they can demand a share of ACG until it runs dry." Instead, the GOTX should concentrate on Serdar-Kapaz

(S-K). Azerbaijan was proposing a 60-40 GOTX-GOAJ joint ownership of this field, with Turkmenistan using Azerbaijani infrastructure to move its oil into BTC. It was unlikely delimitation would be solved for a long time, and as such, in the interim both countries should develop S-K jointly. Azerbaijan "didn't need the money" that it would get from S-K development, but it was important to establish a new form of partnership between the two countries. Additionally, when the two sides agree on joint ownership of S-K, then

"automatically we agree on delimitation." (Comment: Since ACG is west of S-K, GOAJ has previously argued that GOTX agreement on joint S-K ownership perforce means GOTX abandoning its ACG claims.)

¶25. C) Ambassador Mann said that agreement on S-K did not necessarily mean de facto agreement on ACG; Azerbaijan should keep the ACG issue open so that the GOTX and Berdimuhamedov don't lose face. He agreed Azerbaijan had no monetary needs, and that offshore joint energy development with Turkmenistan and Kazakhstan would benefit Azerbaijan strategically. Azerbaijan should focus on practical steps it can take to move forward bilateral cooperation. On S-K, he said that according to what he had heard from experts, if respective islands were not considered in delimitation, S-K would be all in Turkmen territory; if islands were considered then "10-15 percent" was in Azerbaijani territory. He pointed out that in any S-K negotiations, "both sides have to get something out of it," So the actual figure that Azerbaijan could potentially negotiate could be different from the purely technical outcome.

¶26. (C) As for GOTX claims that it only wanted to sell gas at its border, Mann said that in the 1980s Gazprom used to say this, which is where Niyazov picked it up. Berdimuhamedov repeats it as their longstanding default position and perhaps to show his cooperation with Russia. However, while Mann referred to the late Turkmenbashi as one who thought "Moscow put me in this (leadership) position and Moscow can take me out," Berdimuhamedov seems to be interested in pursuing a more balanced foreign policy.

¶27. (C) In response to Mann's question as to whether Aliyev had any specific messages for Berdimuhamedov, Aliyev said that Mann should tell him that Azerbaijan seeks to end disputes borne of the Niyazov era. The GOAJ would consider being a minority owner in S-K, and the GOTX shouldn't stick with its "unrealistic proposals and ridiculous past," which will only block future progress. Azerbaijan is ready to offer its help, and Turkmenistan has already benefited from Azerbaijan and the prospect of an alternative route for Turkmen gas, in the form of higher prices for its gas from Russia. Mann said that Berdimuhamedov has sat through "15 years of meetings" where Turkmenbashi was saying that "Geydar Aliyev is a fox; Azerbaijan is not to be trusted," and as such his reticence to reach out might be understandable.

¶28. (C) COMMENT: Aliyev fully realizes that Azerbaijan's strategic importance significantly increases with the transit of Turkmen gas and Kazakh oil. The GOAJ maintains it has been actively reaching out to Turkmenistan, and now it is time for Berdimuhamedov to show that he is serious in pursuing joint development and is not just using Azerbaijan to extract greater value from Russia. Aliyev is somewhat less realistic in his appraisal of SOCAR's ability to get offshore hydrocarbons out of the ground, whether with ACG Deep Gas or in Umid, according to BP. Azerbaijan's contributions as a gas producer are for the near-term limited to the approximately 12 bcm/a due from SD2 in late 2013. Given the long lead times involved in gas development, if the GOAJ is serious about sending more gas west, it needs to start to prove up its reserves. END COMMENT.

¶28. (U) Ambassador Mann has cleared on this cable
DERSE